STATEMENT OF

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INTRODUCTION

Good morning, my name is Drew Collier, and I am Vice President and General Manager of Agricultural Products for the Union Pacific Railroad. Agricultural Products, which includes Grain and Grain Products, represents approximately 15% of the overall annual revenue to the Union Pacific or nearly $1.5 billion. I have had responsibility for this area since 1989 and have been with the Railroad since 1978.

We have been asked to focus on rail freight service issues, particularly those that are important to Kansas rail shippers. Within this context I would like to touch on a few areas that I believe have relevance. These will include:

- An Overview of Union Pacific's Grain Strategy
- Challenges and Opportunities in Today's Marketplace
- What the Union Pacific is Doing to Meet the Challenges Ahead

To set the stage for this discussion, I believe it is important to reinforce our basic approach to these issues. We come not as an adversary, but as a partner to the grain industry. While we may not always agree on the best course of action, or not always meet the needs of everyone in the logistics chain, we recognize our role as a key supplier and critical element in the grain business.

OVERVIEW OF UNION PACIFIC'S GRAIN STRATEGY

To understand the issues we face, I believe we must first start with our strategy relative to the grain markets we serve. Grain is a core segment of Union Pacific's overall business mix and part of our heritage. The benefit of the mergers of the last several years has been to broaden our grain business so that it now encompasses a good balance of origination and consumptive demand. We also enjoy a good diversity and balance of harvest patterns, starting in late Spring with wheat and progressing thru Fall feed grains harvest. The benefit to our customers of this broad base of grain origination and consumption is improved market reach, flexibility and arbitrage opportunities.

One of the basic elements of our grain strategy is being market responsive . By that I mean that we recognize that we add value to grain merchandising by providing pricing and car allocation strategies that maximize market outlets and alternatives. We attempt to provide clear and consistent rules and programs and then let the market decide where and how the grain should flow. The benefit to the grain shippers and producers is a more efficient market which generally results in improved basis values and margins.

We also include in our strategy grain car allocation programs that ensure fair and equitable distribution. It should be recognized that when the supply of grain competing for transportation exceeds the consumptive demand, as generally happens during harvest or in an inverted market, grain car allocation becomes the marketplace device for allocating profit opportunities. If you view car allocation programs in this light, you can see why the tension over filling car orders can run so high. In reaction to these factors, and with considerable input from our customers, we developed and implemented the Grain Car Allocation System in October of 1996. This system provides four mechanisms for our customers to secure grain cars -- General Distribution, Guaranteed Freight Pools, Vouchers and Contract Trains. These tools have become broadly understood and utilized in the marketplace and are generally regarded as effective.

While we believe this system is responsive to the needs of the marketplace and our customers, we are interested in improving its effectiveness. We are embarking on a review of the Grain Car Allocation System this summer to determine if revisions are warranted. We will solicit input from those involved in using the system. We intend to announce by this Fall what changes, if any, will be made for implementation in October of 1999.

The final point of our grain strategy that I would like to mention is our approach to rewarding productivity. We believe the best and most responsive strategy is to establish rate structures that provide the lowest cost for the most efficient shipment. By providing rates for unit trains, shuttle train incentives and other similar approaches, we share the productivity gains of efficiency. This approach tends to level the playing field among all those willing to invest in efficient facilities, and minimize the leverage of aggregated volume in rate negotiations. In any case, we remain committed to serving all segments of the demand, regardless of unit size, in response to the needs of the market.

CHALLENGES AND OPPORTUNITIES IN TODAY'S MARKETPLACE

The challenges faced by agri-business today are considerable and complex. On the other hand, opportunities for growth and margin improvement are also considerable. Many of these issues involve interaction with the railroads and, in several cases, rail transportation is central to the issue. There are several of these challenges and opportunities worth discussion.

Volatility of demand for rail transportation has been one of the key drivers of the tension between shippers of grain and railroads, going back to the earliest days of both businesses. Volatility in this sense can be defined as that which can not be predicted. To a large degree and over the longer time frame, demand that we can anticipate can be accommodated through capacity expansions. The problem is that we never know from year to year, season to season, what to expect. We recognize that this volatility is a base element of agricultural production and we are not alone in suffering the effects. In the days of redundant capacity, railroads could better react to unexpected surges in demand and redeploy assets to serve the needs of grain shippers. The growth in demand in general for rail transportation, combined with the elimination of redundancy in a drive to lower our costs, has eliminated this capability. The response necessary to increase capabilities -- hiring more people, buying more locomotives, or building more track (all of which we are doing) -- are not short term solutions and do not serve the needs of nearby unexpected demand.

Related to the volatility issue is that of fleet sizing for grain cars. The term you can't build a church for Easter Sunday has been (over)used to describe the grain car fleet dilemma. An alternative description of this issue would be that our customers can't afford the rates necessary to support a fleet sized for peak periods. Cars sitting idle for extended periods has to be considered as a failure cost in cost of quality methodology. A fleet sized for average annual consumptive demand is, in our view, a rational approach. It must be recognized, however, that this will almost always be inadequate to meet peak demand periods.

As important as rail rates are to the viability of the grain business, it must also be recognized that rail transportation is derived demand. Transportation can not create a market where none exists, but logistics capacity can limit how much of the market is captured during peaks. This issue comes into the discussion as seasonal rail rate increases or decreases are suggested as a solution to moderating demand. Our experience is that rail rates can not (or are not allowed to) change as quickly or as dramatically as necessary to meter overall demand to smooth out these peaks.

In spite of these challenges, there are several important opportunities that the industry is addressing. One of these that has received considerable attention is Identity Preserved Grain. This approach proposes to create added value for both the consumer and producer through grains having specialized attributes, e.g. high oil content. Concern has been raised whether the railroads would be able to handle a growth in this segment of the grain business or whether we want only unit trains. We are supportive of the concept of I.P. grain and have some programs in place today which move this type of grain in single cars in manifest service. We do not believe it is an either/or situation -- we should be able to do both. The question that remains, however, is whether the added value of I.P. grain will support the added logistics costs of the necessary handling to make this concept work.

In the category of opportunities I would also add the issue of incentives for more efficient shipments. We have been criticized for forcing investment in shuttle train facilities. We view this not as a requirement, but an opportunity. Our approach is to offer the incentives that reflect our cost savings for these more efficient shipments and let the market decide whether to invest. We believe this approach will reduce the overall cost of getting the grain to market. To ignore these economics by allowing the grain transportation to be priced to the level of the most inefficient shipment configuration will only reduce the competitiveness of our grain on the world market.

WHAT THE UNION PACIFIC IS DOING TO MEET THE CHALLENGES AHEAD

It is to state the obvious that we must first focus on Service Recovery. We need our overall network operating at normal levels of train velocity and fluidity to be able to serve the grain industry and Kansas in the manner that meets their needs. Our struggles in this regard have been well documented and reviewed in numerous forums. I believe it is sufficient to say that we recognize that Service Recovery is our most important and critical challenge, and we are all working as hard as we know how to make that happen.

In addition to our focus on returning the Union Pacific to normal service levels in general, there are several initiatives in place that are specific to grain and our customers in Kansas. One of the most notable is the capital investments we are making on the Kansas Pacific Line that runs through Hays. We started last year, and will continue this year and next with a major project to increase the number of sidings on this line. This line being one of our most important grain gathering lines in Kansas should allow us to handle more grain shipments originating along this line.

One of the other initiatives we are working on is an education program in utilizing the tools available in our Grain Car Allocation System. Working with Tom Tunnel and the Kansas Grain and Feed Association, we are developing a training seminar that will help our customers understand how the risk of car placement can be better managed.

The final area that I will mention is the effort to create a more meaningful dialog regarding expectations and our capabilities. The railroads need better information on demand. Our customers need better information on our capabilities. Policy makers need better information on where real issues exist that need government intervention. We are convinced that through economic, fact-based discussions we can improve understanding in all of these areas. One of the examples of how we are attempting to facilitate this improved dialog is a plan we are working on to share information on our current and historical car loadings of grain via our Internet site.

In this area of improved communication is the dialog we are attempting regarding grain stored on the ground. We are concerned that we may face another situation this Fall with excessive ground storage situations. Storage space is at a premium today, and we are expecting large crops, both in wheat and feed grains. Yet the farmer has not been an active seller this year, and overall grain markets have been very slow. We are setting ourselves up for a situation where some of the grain we harvest will have nowhere to go but on the ground. We expect to be in better shape to handle grain shipments during harvest than we were last year, but the question is whether it will be enough. If the market attempts to liquidate a large portion of the carryover and harvest volume in a short period of time, we will have another crisis.

CONCLUSION

We intend to be positioned to handle grain during this upcoming season in line with our historical capabilities. To accomplish this we expect to have our overall service capabilities back to normal. We believe we have strategies in place that are responsive to the needs of the grain industry. At expected velocity we have a fleet of grain cars that should be adequate to meet the normal demand. Most importantly, we recognize the necessity and have the desire to return to being the reliable supplier and partner to the grain industry that we have demonstrated in the past. We appreciate everyone's patience and support as we work towards those goals.

This concludes my remarks, and I would be happy to answer any questions.